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TAGS: ECON EINV EFIN ETRD BEXP KTDB PGOV SF
SUBJECT: SOUTH AFRICA ECONOMIC NEWSLETTER
April 15 2005 ISSUE

¶1. Summary. Each week, AmEmbassy Pretoria publishes an economic newsletter based on South African press reports. Comments and analysis do not necessarily reflect the opinion of the U.S. Government. Topics of this week's newsletter are:
- Surprise Interest Rate Cut;
- Manufacturing Growth Declining;
- Reserve Bank Slows Accumulation of Foreign Exchange;
- Foreign Tourist Arrivals Drop;
- Treasury Will Spend Tax Revenue Surplus to Reduce Debt;
- Trading Activity Stable; Expectations Still High;
- Commercial Property Confidence Strong; and
- Gautrain Will Increase GDP by R2.6 billion.
End Summary.

SURPRISE INTEREST RATE CUT
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¶2. The South African Reserve Bank's (SARB) Monetary Policy Committee reduced interest rates by 50 basis points to bring the repurchase rate to 7 percent. The prime lending rate should be reduced to 10.5 percent. The Monetary Policy Committee (MPC) noted evidence of slower economic activity in the manufacturing sector as a result of the move by the rand to a higher trading range over the past six months, as noted in the following paragraph. In addition, recent evidence of slowing inflation and inflationary expectations were also cited. The latest inflation expectations survey conducted by the Bureau for Economic Research (BER) at the University of Stellenbosch showed a significant decline in inflation expectations. According to the survey, CPIX inflation expectations reached their lowest level since the BER started the survey in 2000. For the first time, survey respondents expect inflation to be below the upper end of the inflation target band. On average, CPIX inflation is expected to be at 4.5 per cent, the mid-point of the band for 2005, down from 5.5 per cent in the previous survey. CPIX inflation is also expected to remain within the target range for the next 3 years. The reduction in interest rates took most analysts by surprise, as a Reuters poll of 15 economists done last week predicted that the SARB would keep the repurchase rate at 7.50 percent for the remainder of the year, with any rise in 2006 limited to less than 50 basis points. The unexpected rate cut may signal that the SARB is more convinced that oil prices will soon decline and that it is more concerned about the detrimental impact of a strong rand. Source: I-Net Bridge and Standard Bank, MPC Alert, April 14; Business Day April 8.

MANUFACTURING GROWTH DECLINING
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¶3. Manufacturing production growth has sharply decelerated in the first two months of 2005 compared to December's growth of 7.9 percent, according to statistics based on a revised manufacturing sample by Statistics SA. In January, manufacturing production grew by 3.2 percent y/y and February's growth of 2.7 percent continued the trend of slower growth. Slower growth in South African manufacturing production reflects rand strength, poor economic growth in European markets, and impacts of high oil prices on importing countries. Since 35 percent of all South African manufactured exports go to countries in the Euro zone, slower economic growth and increased European spending on higher energy costs have restrained manufacturing export growth. Manufacturing production continues to grow due to strong local consumer demand. Consumer demand is expected to remain strong in 2005, as the recent R6.8 billion income tax rebates and expectations of stable interest rates should support local demand. On a quarterly basis, manufacturing production declined 0.6 percent, with 7 out of 10 manufacturing sectors reporting a decline in output. Food and beverage sector showed the largest quarterly production decline of 0.5 percent, followed by wood and paper products and basic iron and steel. Manufacturing sales showed the same

decelerating growth as production, with the first two months' growth in 2005 at 4.9 percent and 4.3 percent, respectively. Source: Standard Bank, Manufacturing Unpacked and Statistics SA Release P0341.2, April 14.

¶4. Comment. The April 14th release of Stats SA in manufacturing sales and production used a new sample for the first time, based on an improved business register, created in July 2004, which included more small businesses that were not required to register for the VAT. The trends in the new survey results mirror those of the old survey despite recording a 2.6 percent higher level in manufacturing sales. End Comment.

RESERVE BANK SLOWS ACCUMULATION OF FOREIGN EXCHANGE
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¶5. The South African Reserve Bank's (SARB) accumulation of foreign exchange reserves slowed significantly in March, as the rand weakened almost 7 percent against the dollar. Net foreign exchange and gold reserves, also known as the international liquidity position, increased to $12.4 billion from $12.2 billion in February, an increase of $194 million compared with February's increase of $527 million. It was the 14th consecutive month that net reserves increased; they are almost double what they were a year ago. Until recently, South Africa had the lowest reserves among its emerging-market peers. Its improved reserve position has contributed to last year's sovereign credit rating upgrade by Moody's. Source: Business Day, April 8.

FOREIGN TOURIST ARRIVALS DROP
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¶6. Foreign tourist arrivals dropped 2 percent (y/y) in November 2004, according to Statistics SA (Stats SA), due to high oil prices making air travel more expensive and the strong rand. South Africa is no longer an inexpensive destination. The reduction in foreign tourists poses a threat to South Africa's tourism industry, which employs about 500,000 people and contributes 7.1 percent to gross domestic product. November was the first month showing negative y/y growth. The number of international tourists to SA increased 5 percent in October 2004, compared with the previous year. Tourists from Germany, France and the U.K., the top sources of South African visitors, declined 4.3 percent, 23 percent, and 2.5 percent, respectively. The number of visitors from the rest of Africa rose 8.9 percent in November. More than 92 percent of these were from six neighboring countries, including Lesotho and Swaziland. Source: Business Day, April 13.

TREASURY WILL SPEND TAX REVENUE SURPLUS TO REDUCE DEBT
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¶7. Government's R9.6 billion tax surplus raised in the 2004-05 fiscal year would be used to repay government debt maturing this year, according to National Treasury Director-General Lesetja Kganyago. The statement ends the debate over what should be done with the excess. The Congress of South African Trade Unions had proposed that it be used to fund infrastructure development. Kganyago told Parliament's Finance Committee that the windfall could not be used for other government expenditure this year because the 2005-06 budget had already been prepared and tabled before revenue collection figures were finalized by the South African Revenue Service. Repaying debt would reduce debt-servicing costs and release resources to other areas of expenditure. About R29 billion in national debt matures this fiscal year, mainly R152 bonds. By using the R9.5 billion to settle part of this debt, government's total borrowing requirement would be reduced. The net public sector borrowing requirement this fiscal year has been estimated by national treasury at R53 billion compared with last year's R38 billion. The targeted mix of 20 percent foreign government debt and 80 percent local debt had been reviewed, with the Treasury deciding not to increase the foreign debt significantly because the risks arising from currency volatility were too great. Currently, foreign debt represents only 13.5 percent of all government debt. The Treasury plans to borrow up to $1.5 billion on foreign markets so as to avoid crowding out the domestic capital market. Taking into account a redemption of $200-$300 million in foreign debt, net foreign budgeted borrowing should be $1.3 billion. This move will allow state-owned enterprises to more easily raise additional funds for infrastructure projects on the local market. Source: Business Day, April 13.

TRADING ACTIVITY STABLE; EXPECTATIONS STILL HIGH
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¶8. March's South African Trade Management Indices (SATMI)

showed current trading conditions improved slightly from February's level although expectations for the next six months remained high. The index for current trading conditions reached 49.1, still below the 50 level, signaling that trading conditions have slightly deteriorated compared to February. According to SATMI's trading index, trading conditions were best in November 2004, reaching 55.7, only to have gradually retreated each month since. The trade expectations index, measuring expectations for trade conditions for the next six months, reached 63, showing an optimistic view of the medium-term outlook. In both the activity and expectations indices, the employment component signals that a majority of respondents have increased job opportunities. This is the first time both current and expected employment has shown increases. Source: Standard Bank, SATMI, April 7; Business Day, April 8.

COMMERCIAL PROPERTY CONFIDENCE STRONG
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¶9. South Africa's commercial and industrial property market should experience rising lease values, declining vacancies, and more tenants in the next six months, according to eProp's Commercial Property Confidence Index (CPCI). eProp's CPCI for March 2005 reveals that 75 percent of respondents are looking forward to improved business conditions in the short-term. Eighty-one percent of respondents think that lease values will rise in the next six months and more than 70 percent predict rising occupancies. More than 20 percent expect to hire more staff. The CPCI tracks the sentiment of a sample of property managers, asset and portfolio managers, and brokers. Respondents rate their expectations of ten market factors that are unique to commercial property, including number of leases and sales; value of leases and sales; net operating income; rental and vacancy levels; capitalization rates and staff employed. A more general category is sentiment about the management of the public environment. eProp is a research firm devoted to the commercial property market. Source: I-Net Bridge, April ¶13.

GAUTRAIN WILL INCREASE GDP BY R2.6 BILLION
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¶10. The Gautrain Rapid Rail Link project, a proposed high speed commuter rail service linking Johannesburg and Tshwane (Pretoria), will create 1,200 permanent jobs and contribute about R2.6 billion ($426 million, using 6.1 rands per dollar) to South Africa's gross domestic product (GDP), according to a study released by Brait financial service company. The Gautrain will have a ripple effect on the economy by creating 70,000 jobs during the construction phase and another 40,000 jobs when the rail service is operational. The study points to other benefits of Gautrain, such as reduction in congestion, medical costs, and traffic accidents as commuters shift to the rail service. Estimated savings to the economy should reach R15.3 million ($2.6 million). Source: Business Day, April 13.

FRAZER